

Tax Related Guidance for Child Care Providers Webinar

Licensing Requirements

- **Childcare providers regulated by states**
- **State's licensing requirements differ**
- **Visit the Website for the National Resource Center for Health and Safety in Child Care and Early Education**

Child Care Provider Types

- Some small family-related instances may operate without a license, but still considered a business
- In-home care provided by paid housekeeper, maid, governess, etc. - considered a household employee, reported on Sch. H

Recordkeeping

- All businesses required to maintain adequate records of income and expenses
- IRS does not dictate method, but requires records be maintained and kept
- Recordkeeping includes reasonable method of allocating costs between business and personal use

Income

- **Contracts specifying charges, terms of care and responsibilities of provider and client should be kept as records**
- **May be formal document or informal statements reflecting rates, other considerations, and extra charges (see below)**
 - **Diaper charges**
 - **Late pick up or early drop off fees**
 - **Transportation costs**
 - **Registration fees**

Income – Other Charges/Fees

- Payments for absences due to illness or vacation
- Fees to reserve position prior to coming to facility
- Days of operation and closures for holidays, vacations, bad weather days, where payment is due

Required Information Provided to Clients

- Childcare provider's name
- Address
- Tax identification number

or may choose to use Form W-10 as
alternate option

USDA

Food Reimbursement Program

The United State Department of Agriculture provides reimbursement to day care providers through the Child and Adult Care Food Program

IRC §162: Expense

For an expense to be deductible for tax purposes by a business, per IRC §162

- **Business must be for profit activity**
- **Expense must be ordinary and necessary**

IRC §262: Personal Expense

- Only business use portion may be deductible expense, for both personal and business use
- Reasonable method of allocation must be made to determine business usage portion
- Amounts spent for personal or family reasons are **not** deductible business expenses.

Special Tax Laws

- Tax laws contain specific rules in areas where business expenses are difficult to separate from personal expenses
- Childcare industry contains many instances where there is both personal and business use

IRC §280A(c)(4) & (5)

- Provides special method for computing business use percentage of home available only for day care service providers
- Changes exclusive use provision to regular use to qualify for deduction
- Also provides limitation on deduction based on gross income

Revenue Procedure 2003-22

- Provides simplified recordkeeping requirement, optional standard meal and snack rate
- Use for calculating deductible cost of food in lieu of actual costs

IRC 280F

- Additional limitation for total amount of depreciation allowable for each year for passenger automobiles, adjusted annually for inflation
- See Publication 463, *Travel, Entertainment, Gifts and Car Expenses*

IRC §274(d)

- **Must be able to substantiate certain elements of expenses for travel, entertainment, gift, transportation or listed property items such as VCRs, computers claimed as deduction**
- **Include:**
 - Amount
 - Time
 - Place or description
 - Business purpose
 - Business relationship for some cases

Elements of Vehicle Expense

- Cost of vehicle and any improvements
- Date put in use for business purposes
- Mileage for each business use
- Total miles annually
- Date of use of vehicle
- Business destination, and
- Business purpose of expense

Vehicle Expense (Continued)

Rev. Proc. 2010-51 prohibits the use of the standard mileage rate for any automobile for which a taxpayer has claimed a deduction using a method of depreciation other than straight line, a §179 deduction, or any other additional first year depreciation.

IRC §274(d)

Treasury Regulation 1.274-5T explains the elements in detail with examples for the four categories of expenses covered by the Internal Revenue Code 274(d).

Food Expenses

You may:

- Deduct 100% of actual cost of food consumed by your daycare recipients, or
- Use standard meal and snack rates

You may *not*:

- Deduct cost of food consumed by you or your family

Food Expenses (Continued)

See Publication 587, *Business Use of Your Home*, for substantiation computation for total amount deducted

- Eligibility qualifications,**
- Rates, and**
- Records that must be maintained**

Various Supplies

- Supplies may include games, books, child proofing devices and toys.
- Most can be expensed.
- Other more expensive/longer lasting toys may need to be depreciated or expensed under IRC §179.

Business Use of Home

IRC §280A(c)(4)) qualifications:

- **Be in trade or business of providing daycare for children, persons age 65 or older, or persons who are physically or mentally unable to care for themselves.**
- **Have applied for, been granted, or be exempt from having, a license, certification, registration, or approval as daycare center or as family or group daycare home under state law.**

Business Use of Home (Continued)

- **Provision changes “exclusive use” requirement to “regular use” requirement, and provides special formula for computing business percentage**
- **“Regular use” is portion used for business on a continuous, ongoing or recurring basis**

Business Use of Home (Continued)

- **Business percentage computed by multiplying space percentage and time percentage**
- **Space percentage consists of area regularly used for business divided by area of complete home**
- **Time percentage, total number of hours facility was used for childcare business during year divided by total hours in year (8,760)**

Business Use of Home (Continued)

- **Per IRC §280A(c)(5)), deduction for certain expenses for business use of home is limited, if gross income from business use of home is less than total business expenses**
- **Unallowed expenses may be carried over to next year**

Depreciation

- **Allows taxpayer to recover cost or other basis of certain property**
- **Annual allowance for wear and tear, deterioration, or obsolescence for items having useful life of one year or longer**

Depreciation (Continued)

- In service in purchase year, basis for depreciation is generally cost
- Prior to putting property in service in your business, was used for *personal purposes*, the basis for depreciation is lower of cost or fair market value on date put in service

Depreciation (Continued)

Special provisions available to deduct cost of property faster as follows:

- **IRC §179 allows some qualifying assets to have cost or part of cost expensed in year of purchase rather than depreciated**
- **Bonus first year depreciation or special depreciation allowances may be available for periods of time or for special areas, such as federally-declared disaster areas**

Listed Property Limitations

- **§179 deduction and special depreciation allowance for listed property**
 - **Use GDS and declining balance method, if property meets business-use requirement**
- **Listed property must be used predominantly (more than 50% of its total use) for qualified business use to meet requirement**

Listed Property Limitations (Continued)

If property does not meet the (over 50%) rule for qualified business use then:

- **It would not qualify for §179 in year placed in service, and**
- **It would not qualify for special depreciation allowances, including bonus depreciation**

Listed Property Limitations (Continued)

- **Depreciation must be figured using straight line method over ADS recovery period**
- **Excess depreciation on property previously used for over 50% qualified business use must be recaptured (included in income) in first year in which it is no longer used for that business percentage use**

Sale of Home / Capital Gain

If home used in your business and you have a gain which qualifies for exemption from taxation under IRC §121, the portion of allowed depreciation or allowable for periods after May 6, 1997, are *not* tax-exempt.

Summary

- **Some sources of income are unique to childcare providers; i.e. food reimbursement**
- **Records must be kept, including income, expense and usage records**
- **Various expenses and depreciation items**
- **Capital gain and use of home rules**

IRS.gov References

Visit IRS.gov, search Keyword:

- Child Care Tax Center**
- Recordkeeping**
- Child Care Provider Audit Techniques Guide**
- Form 8829 and instructions**

IRS.gov Publications

- Publication 463, Travel, Entertainment, Gift and Car Expenses
- Publication 523, Selling Your Home
- Publication 535, Business Expenses
- Publication 583, Starting a Business and Keeping Records
- Publication 587, Business Use of Your Home
- Publication 946, How to Depreciate Property

Other Website References

- **USDA.gov @
www.fns.usda.gov/cnd/care/**
- **National Resource Center for Health
and Safety in Child Care and Early
Education @
nrckids.org/STATES/states.htm**